

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF HAWAII

In the Matter of the Application of)  
                    KAUPULEHU WATER COMPANY        )  
  )  
For a Change in Rates and Other        )  
Approvals.    )  
\_\_\_\_\_

DOCKET NO. 05-0124

DECISION AND ORDER NO. 22178

Filed Dec. 9, 2005  
At 2:25 o'clock P .M.

Karen Higashi.  
Chief Clerk of the Commission

ATTEST: A True Copy  
KAREN HIGASHI  
Chief Clerk, Public Utilities  
Commission, State of Hawaii.

K. Higashi.

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF HAWAII

|                                      |                              |
|--------------------------------------|------------------------------|
| In the Matter of the Application of) |                              |
| KAUPULEHU WATER COMPANY )            | Docket No. 05-0124           |
| For a Change in Rates and Other )    | Decision and Order No. 22178 |
| Approvals. )                         |                              |
| _____ )                              |                              |

DECISION AND ORDER

By this Decision and Order, the commission approves the transfer of two (2) deep water wells (Wells 3 and 4), a water treatment plant, and a water reservoir, as described in greater detail below, from Kaupulehu Makai Venture to KAUPULEHU WATER COMPANY ("KWC"), in accordance with Hawaii Revised Statutes ("HRS") § 269-19.5(c).

I.

Background

A.

Procedural History

KWC requests commission approval of the transfer from Kaupulehu Makai Venture to KWC of two (2) Deep Water Wells (Wells 3 and 4), a Water Treatment Plant, and 413' Reservoir, all as described in the Application (collectively, the "Facilities").<sup>1</sup>

---

<sup>1</sup>KWC's Application, Exhibits A - H, Verification, and Certificate of Service, filed on May 24, 2005; and KWC's Amended Certificate of Service, filed on June 13, 2005 (collectively, the "Application"). On June 17, 2005, the commission bifurcated KWC's request to transfer the facilities from its other requests

KWC makes its request pursuant to HRS §§ 269-16(b), 269-17, and 269-19.5.<sup>2</sup>

KWC served copies of its Application upon the Department of Commerce and Consumer Affairs, Division of Consumer Advocacy ("Consumer Advocate").<sup>3</sup> KWC responded to: (1) the Consumer Advocate's information requests on August 22, 2005, and September 22, 2005; and (2) the commission's information requests on September 13, 2005, and November 14, 2005, respectively.<sup>4</sup>

On October 31, 2005, the Consumer Advocate filed its Statement of Position, and stated that it did not object to the transfer of the Facilities to KWC.<sup>5</sup> On December 2, 2005, KWC filed its Statement of Position and Supplemental Written

---

involving proposed changes to its tariff, including the commission's approval to: (1) establish an initial rate for non-potable reject water; and (2) increase KWC's water consumption charge for potable water. See Order No. 21878, filed on June 17, 2005. KWC utilizes a July 1, 2005 to June 30, 2006 test year ("test year").

<sup>2</sup>KWC cites to HRS § 269-16(b) as part of its request to change certain of its tariff provisions, which the commission intends to address in a forthcoming Decision and Order. HRS §§ 269-17 and 269-19.5 are discussed in Section IV of this Decision and Order, involving the transfer of facilities.

<sup>3</sup>KWC and the Consumer Advocate are collectively referred to as the "Parties."

<sup>4</sup>The Consumer Advocate's initial set of information requests inadvertently uses two (2) designations of CA-IR-23 and CA-IR-24, respectively, and KWC's responses to these information requests refer to these same duplicate designations. The commission, on its own motion, corrects the mislabeled designations such that the Consumer Advocate's initial information requests now run from CA-IR-1 to CA-IR-31.

<sup>5</sup>Consumer Advocate's Statement of Position, filed on October 31, 2005, as amended on November 8, 2005 (collectively, "Statement of Position").

Testimony,<sup>6</sup> in response to the Consumer Advocate's Statement of Position.

This Decision and Order addresses the proposed transfer of the Facilities from Kaupulehu Makai Venture to KWC.

B.

The Application

1.

Kaupulehu Water Company

KWC is a Hawaii limited partnership: (1) ninety-nine percent (99%) owned by Kaupulehu Makai Venture, a California general partnership; and (2) one percent (1%) owned by Kaupulehu Utility Corporation, a Hawaii corporation.<sup>7</sup> Kaupulehu Utility Corporation is the general partner, while Kaupulehu Makai Venture is the limited partner. Kaupulehu Utility Corporation has the sole and exclusive right to manage KWC.

KWC holds a certificate of public convenience and necessity ("CPCN") to provide water utility service within the service area of Kaupulehu, island of Hawaii.<sup>8</sup> KWC states that, following the issuance of its CPCN in 1996, Kaupulehu Makai

---

<sup>6</sup>KWC's Statement of Position, Supplemental Written Testimony, Exhibits A and 1, and Certificate of Service, filed on December 2, 2005.

<sup>7</sup>Kaupulehu Makai Venture and Kaupulehu Utility Corporation are both owned by Kajima Kona Company, Inc., ultimately owned by Kajima Holdings, Inc. See KWC's response to CA-IR-5(c).

<sup>8</sup>See Docket No. 94-0300, Decision and Order No. 14649, filed on April 26, 1996; Order No. 14758, filed on July 1, 1996; and Order No. 15333, filed on January 24, 1997.

Venture transferred certain water system improvements to KWC in exchange for additional capital interests in KWC.

2.

KWC's Water System

KWC's water system presently consists of facilities owned by KWC and Kaupulehu Makai Venture. The facilities owned by KWC include: (A) two (2) deep water wells (Wells 1 and 2); (B) three (3) reservoirs with a total storage capacity of 1,020,000 gallons; (C) transmission lines; (D) a pressure reducing system; and (E) electric and telephone systems. The Facilities owned by Kaupulehu Makai Venture are: (A) Wells 3 and 4; (B) a Water Treatment Plant; and (C) 413' Reservoir.

KWC initially provided water service to its customers using two (2) deep water wells (Wells 1 and 2) and related storage and transmission facilities originally constructed by Kaupulehu Makai Venture. The capacity of each well is approximately 526,400 gallons per day ("gpd"), with one (1) of the two (2) wells designated as a back-up well. In 1994, when KWC applied for its CPCN, its projected average daily consumption for the years 2000, 2001, and 2002 was 456,901 gpd, 522,901 gpd, and 583,701 gpd, respectively.

Presently, the average daily consumption by KWC's customers is approximately 940,000 gpd, with the average daily consumption projected to "increase to approximately 1,033,000

gallons per day by July 1, 2005 and to 1,210,000 gallons per day by June 30, 2006."<sup>9</sup>

KWC's "water source requirements must also take into account the need for treatment of the water which results in the loss of approximately 25% of the water initially pumped from [KWC's] wells."<sup>10</sup>

a.

Wells 3 and 4

KWC states that:

1. KWC addressed its need for additional sources of water by entering into two (2) Standby Water Supply Agreements with Kaupulehu Makai Venture, enabling KWC to operate and receive potable water from two (2) deep water wells owned by Kaupulehu Makai Venture: Well 3 (540,000 gpd) and Well 4 (720,000 gpd).

2. KWC pays Kaupulehu Makai Venture a per thousand gallons ("TG") charge for the water taken plus the general excise tax to reimburse Kaupulehu Makai Venture for: (A) the depreciation on Kaupulehu Makai Venture's capital investment in the two (2) wells, related transmission lines, and other facilities; and (B) Kaupulehu Makai Venture's cost of funds for such capital investment. KWC is also responsible for paying for all operating, maintenance, and other costs required for the production and delivery of water from Kaupulehu Makai Venture's two (2) wells.

---

<sup>9</sup>KWC's Application, at 4.

<sup>10</sup>KWC's Application, at 4.

3. Kaupulehu Makai Venture agrees to transfer its two (2) wells to KWC "for value in exchange for additional partnership interests in [KWC] and not as contributions in aid of construction."<sup>11</sup>

KWC requests the commission's approval to transfer Kaupulehu Makai Venture's two (2) wells, the related transmission lines, and other facilities, to KWC, "in amounts equal to [Kaupulehu Makai Venture's] original capital investments in Well Nos. 3 and 4[,] less straight-line depreciation[,] " in exchange for additional partnership interests in KWC.<sup>12</sup>

b.

Water Treatment Plant

KWC states that:

1. The water from KWC's existing wells and Kaupulehu Makai Venture's two (2) wells contains high levels of suspended solids, including silicates, which aggressively corrode KWC's copper pipelines as well as those installed by KWC's hotel, condominium, residential, and commercial customers.

2. KWC addresses the corrosion problem by treating the water in a Water Treatment Plant constructed by Kaupulehu Makai Venture, utilizing a reverse osmosis process. KWC operates the Water Treatment Plant pursuant to a Water Treatment Plant Agreement with Kaupulehu Makai Venture.

---

<sup>11</sup>KWC's Application, at 5.

<sup>12</sup>KWC's Application, at 5.

3. KWC is responsible for: (A) all costs and expenses of operating, maintaining, and repairing the Water Treatment Plant; and (B) paying Kaupulehu Makai Venture an amount equal to: (i) the straight-line depreciation on Kaupulehu Makai Venture's capital investment in the Water Treatment Plant; (ii) a return to Kaupulehu Makai Venture on the undepreciated amount of such capital investment; plus (iii) the general excise tax.

4. The Water Treatment Plant produces approximately 344,000 gpd of non-potable reject water suitable for the irrigation of landscaping and golf courses within KWC's service area.<sup>13</sup>

5. Kaupulehu Makai Venture agrees to transfer the Water Treatment Plant to KWC "for value in exchange for additional partnership interests in [KWC] and not as a contribution in aid of construction."<sup>14</sup>

KWC requests the commission's approval to transfer Kaupulehu Makai Venture's Water Treatment Plant to KWC, "in an amount equal to [Kaupulehu Makai Venture's] original capital investment in the Water Treatment Plant[,] less straight-line

---

<sup>13</sup>Presently, irrigation water for landscaping and golf courses within KWC's service area is drawn from non-potable wells owned and operated by Kaupulehu Makai Venture. However, Kaupulehu Makai Venture has agreed to accept the non-potable reject water from the Water Treatment Plant, which, after dilution with brackish water, will be used for landscape and golf course irrigation purposes. Accordingly, as part of the bifurcated rate case, KWC seeks to establish a rate of \$0.75 per TG, for the non-potable reject water produced by the Water Treatment Plant.

<sup>14</sup>KWC's Application, at 6.



depreciation[,]" in exchange for additional partnership interests in KWC.<sup>15</sup>

C.

413' Reservoir

KWC explains that:

1. KWC currently owns three (3) reservoirs with a total storage capacity of 1,020,000 gallons. "Based on the increased water sources required for [KWC's] service area, additional storage of approximately 500,000 gallons [is] required."<sup>16</sup> In order to obtain this additional storage capacity, KWC entered into a Reservoir Agreement with Kaupulehu Makai Venture.

2. KWC operates Kaupulehu Makai Venture's 413' Reservoir, which has a storage capacity of 500,000 gallons.

3. KWC is responsible for: (A) all costs and expenses of operating, maintaining, and repairing the 413' Reservoir; and (B) paying Kaupulehu Makai Venture an amount equal to: (i) the straight-line depreciation on Kaupulehu Makai Venture's capital investment in the 413' Reservoir; (ii) a return to Kaupulehu Makai Venture on the undepreciated amount of such capital investment; plus (iii) the general excise tax.

4. Kaupulehu Makai Venture agrees to transfer the 413' Reservoir to KWC "for value in exchange for additional

---

<sup>15</sup>KWC's Application, at 6.

<sup>16</sup>KWC's Application, at 6.

partnership interests in [KWC] and not as a contribution in aid of construction."<sup>17</sup>

KWC requests the commission's approval to transfer the 413' Reservoir to KWC, "in an amount equal to [Kaupulehu Makai Venture's] original capital investment in the 413' Reservoir[,] less straight-line depreciation[,] " in exchange for additional partnership interests in KWC.<sup>18</sup>

### 3.

#### Summary

The two (2) Standby Water Supply Agreements, Water Treatment Plant Agreement, and Reservoir Agreement are part of the docket record.<sup>19</sup> Each contract includes a provision stating that the Agreement will continue in effect until KWC obtains an order from the commission authorizing Kaupulehu Makai Venture to transfer the subject asset to KWC for value in exchange for

---

<sup>17</sup>KWC's Application, at 7.

<sup>18</sup>KWC's Application, at 7.

<sup>19</sup>See KWC's response to PUC-IR-101(A) to (D): (1) Kaupulehu Standby Water Supply Agreement between Kaupulehu Makai Venture and KWC, for Well 3, effective January 1, 2001; (2) Kaupulehu Standby Water Supply Agreement between Kaupulehu Makai Venture and KWC, for Well 4, dated December 16, 2004, effective June 1, 2003; (3) Kaupulehu Water Treatment Plant Agreement between Kaupulehu Makai Venture and KWC, effective February 12, 2002; and (4) Kaupulehu Reservoir Agreement between Kaupulehu Makai Venture and KWC, dated December 16, 2004, effective January 1, 2003. Hereinafter, each contract is individually referred to as the "Agreement" and collectively as the "Agreements."

additional partnership interests in KWC and not as a contribution-in-aid-of-construction ("CIAC").<sup>20</sup>

In sum, KWC seeks the commission's approval to transfer Kaupulehu Makai Venture's two (2) wells, the Water Treatment Plant, and the 413' Reservoir, to KWC, in exchange for additional partnership interests in KWC. The net book values of Well 3, Well 4, the Water Treatment Plant, and the 413' Reservoir, as of July 1, 2005, the beginning of KWC's test year, are \$1,406,302, \$2,040,850, \$3,729,978, and \$1,527,256, respectively, for a total of \$8,704,386.<sup>21</sup> For KWC's rate case, the Facilities are valued at \$8,419,319 (average rate base).<sup>22</sup>

#### C.

##### Consumer Advocate's Position

The Consumer Advocate focused its review on the two (2) issues identified by the Parties in Stipulated Procedural Order No. 21943, filed on July 22, 2005:

1. Whether the proposed transfer of the third and fourth Deep Water Wells, Water Treatment Plant, and the 413' Reservoir from Kaupulehu Makai Venture to KWC is reasonable.

---

<sup>20</sup>See: (1) Kaupulehu Standby Water Supply Agreement between Kaupulehu Makai Venture and KWC for Well 3, Recital D and Paragraph 1, Term of Agreement; (2) Kaupulehu Standby Water Supply Agreement between Kaupulehu Makai Venture and KWC for Well 4, Recital D and Paragraph 1, Term of Agreement; (3) Kaupulehu Water Treatment Plant Agreement, Recital E and Paragraph 1, Term of Agreement; and (4) Kaupulehu Reservoir Agreement, Paragraph 1, Term of Agreement.

<sup>21</sup>See KWC-CA-IR-4.

<sup>22</sup>See KWC's Supplemental Exhibit H; and KWC-PUC-IR-202.

2. If yes, whether the terms of the proposed transfer of the third and fourth Deep Water Wells, Water Treatment Plant, and the 413' Reservoir from Kaupulehu Makai Venture to KWC are reasonable.

1.

Need for the Transferred Facilities

The Consumer Advocate assessed KWC's anticipated need for each of the Facilities in its water utility operations, noting that the proposed transfer "will allow KWC to acquire assets for the provision of the regulated service and include the costs of the acquired assets in [KWC's] rate base."<sup>23</sup>

a.

Wells 3 and 4

The Consumer Advocate states that:

1. The capacity of each of KWC's wells (Wells 1 and 2) is approximately 526,400 gpd, with one (1) well designated as a back-up well. At the time of the commission's issuance of KWC's CPCN in April 1996, KWC's projected average daily water consumption for the calendar years 2000, 2001, and 2002 was 456,901 gpd, 522,901 gpd, and 583,701 gpd, respectively. "Thus, there appeared to be sufficient capacity with Well Nos. 1 and 2 to serve KWC's customers' needs through the year 2002."<sup>24</sup>

---

<sup>23</sup>Consumer Advocate's Statement of Position, at 7.

<sup>24</sup>Consumer Advocate's Statement of Position, at 7 - 8.

2. The average daily water consumption by KWC's customers is presently estimated at 940,000 gpd. For the 2006 test year, KWC estimates 1,033,224 gpd in water sales, with the average daily consumption expected to increase to approximately 1,210,000 gpd by June 30, 2006, the end of its test year.

3. KWC's two (2) existing wells (Wells 1 and 2) are able to produce 1,052,800 gpd of water, of which approximately twenty-five (25) percent is rejected following reverse osmosis treatment at the Water Treatment Plant. Thus, KWC is left with a capacity of 789,600 gpd using its two (2) existing wells. This amount, moreover, "does not consider any water that is normally lost in the transmission and distribution system and does not reflect the use of one well as a 'back-up.'"<sup>25</sup>

4. Under the Consumer Advocate's analysis:

A. "[T]here clearly is insufficient capacity with only Well Nos. 1 and 2 to meet [KWC's] test year water sales projections that reflect KWC's customers' water needs. As a result, KWC must acquire additional sources of water, namely from Well Nos. 3 and 4 to meet [KWC's] customers' needs."<sup>26</sup>

B. "Although KWC may not presently need the entire capacity of Well Nos. 3 and 4, there appears to be only 14% of excess capacity, or 255,698 gpd available to meet the water

---

<sup>25</sup>Consumer Advocate's Statement of Position, at 8 (footnote and text therein omitted). In its review of the pertinent data, the Consumer Advocate notes that KWC experiences, on average, a system water loss factor of ten (10) percent.

<sup>26</sup>Consumer Advocate's Statement of Position, at 8 - 9.

consumption demands of new customers expected to require service beyond the test year."<sup>27</sup>

The Consumer Advocate concludes that: (1) KWC appears to need the capacity provided by Wells 3 and 4; thus (2) the proposed transfer of both wells to KWC is reasonable.

b.

Water Treatment Plant

The Consumer Advocate recognizes that the water drawn from KWC's existing wells (Wells 1 and 2) and Kaupulehu Makai Venture's wells (Wells 3 and 4) must undergo treatment at the Water Treatment Plant to remove high levels of suspended solids which corrode KWC's and its customers' copper pipelines. "Thus, it appears that the proposal to transfer ownership in the treatment facility is reasonable since the water pumped from the four wells requires treatment."<sup>28</sup>

---

<sup>27</sup>Consumer Advocate's Statement of Position, at 9. The fourteen (14) percent excess capacity figure is based on the Consumer Advocate's calculations at page 9 of its Statement of Position. Utilizing the capacity of all four (4) wells and with Well 2 as a standby, back-up well, the Consumer Advocate calculates KWC's test year utilization factor at eighty-six (86) percent.

<sup>28</sup>Consumer Advocate's Statement of Position, at 11.

c.

#### 413' Reservoir

The State of Hawaii, Water System Standards (2002), as enforced by the County of Hawaii, Department of Water Supply, provides in part:<sup>29</sup>

##### **111.07 RESERVOIR CAPACITY**

Reservoir shall be sized as follows:

1. Meet maximum day consumption. Reservoir full at the beginning of the 24-hour period with no source input to the reservoir.
2. Meet maximum day rate plus fire flow for duration of fire. Reservoir  $\frac{3}{4}$  full at start of fire, with credit for incoming flow from pumps, one maximum size pump out of service.
3. Minimum size reservoir shall be 0.1 [million gallons]. . . . .

Where there are two or more reservoirs serving the same system, the design shall be made on the basis of combined protection provided by all facilities available.

The Consumer Advocate states that:

1. KWC presently has three (3) reservoirs with a total storage capacity of 1,020,000 gallons. In addition, based on KWC's test year projections, the average daily consumption of water is expected to be 1,033,224 gpd. Thus, the assumed maximum daily consumption is expected to be 1,549,837 gpd.<sup>30</sup>

---

<sup>29</sup>See Consumer Advocate's Statement of Position, at 9 - 10. See also [www.hawaiidws.org/econ/Water%20System%20Standards%202002%20amendment%201.pdf](http://www.hawaiidws.org/econ/Water%20System%20Standards%202002%20amendment%201.pdf).

<sup>30</sup>The assumed maximum daily consumption is calculated by multiplying the average daily consumption of 1,033,224 gpd by 1.5. In a telephone conversation between the Consumer Advocate's Office and an engineer with the County of Hawaii, Department of Water Supply, Planning Division, "the Consumer Advocate was informed that the standard for purposes of calculating the reservoir requirements is to assume that the daily peak

2. KWC will need an additional 500,000 gallons of storage, or a total of 1,500,000 gallons of storage to meet the first criteria under Section 111.07. KWC is able to obtain the additional 500,000 gallons of storage from the 413' Reservoir. Accordingly, it appears that the proposed transfer of the 413' Reservoir to KWC is reasonable.

2.

Terms of the Proposed Transfer

The Consumer Advocate believes that the terms for the proposed transfer of the Facilities to KWC are reasonable and do not appear to adversely affect KWC's ratepayers.

Specifically:

1. Each Agreement includes a provision which states that the Agreement will continue in effect until KWC obtains an order from the commission authorizing the transfer of the Facilities to KWC for value in exchange for additional partnership interests in KWC, as opposed to CIAC. "Thus, it appears that [Kaupulehu Makai Venture] intended to eventually transfer ownership in these facilities to KWC."<sup>31</sup>

2. KWC is responsible for paying for all operating, maintenance, and repair costs of the Facilities pursuant to the terms of each Agreement. The operating and maintenance ("O&M") costs for each of the Facilities are recorded in KWC's O&M

---

consumption will be approximately 1.5 times the average daily consumption." See Consumer Advocate's Statement of Position, at 10, footnote 7.

<sup>31</sup>Consumer Advocate's Statement of Position, at 13.



expenses. "Thus, the costs to operate and maintain these assets are already reflected in the test year revenue requirements and no additional operating or maintenance costs [are] expected to be incurred solely as a result of the proposed transfer of assets."<sup>32</sup>

3. In addition, regardless of who owns the Facilities, KWC's ratepayers must pay for the annual straight-line depreciation on the Facilities, a return on the average undepreciated plant costs (i.e., a return on the net book value of the plant at KWC's most current cost of capital), and the general excise taxes, pursuant to the terms of the Agreement

4. Kaupulehu Makai Venture proposes to transfer the Facilities as an equity contribution. If the proposed transfer is approved by the commission, the Facilities will be valued at their net book values, based on straight-line depreciation up through the date of the transfer. This proposed treatment of the transfer of Facilities is consistent with the commission's treatment of KWC's initial water facilities in Docket No. 94-0300, In re Kaupulehu Water Co.<sup>33</sup>

5. In sum, "[r]atepayers will pay for approximately the same costs regardless of who owns the facilities since KWC is required to pay for the operating and maintenance costs, the annual straight-line depreciation and a return on the

---

<sup>32</sup>Consumer Advocate's Statement of Position, at 13.

<sup>33</sup>In Docket No. 94-0300, the commission amended Decision and Order No. 14649, filed on April 26, 1996, by including KWC's plant costs of \$9,960,618 in the utility's rate base, as part of KWC's application for a CPCN and approval of its initial water rates. See Order No. 15333, filed on January 24, 1997.

undepreciated cost of the assets and revenue taxes associated with such payments."<sup>34</sup>

## II.

### Discussion

#### A.

#### HRS § 269-17

In addition to HRS § 269-19.5, KWC seeks the commission's approval to transfer the Facilities from Kaupulehu Makai Venture pursuant to HRS § 269-17.

HRS § 269-17 provides that, upon the commission's prior approval, a public utility corporation may issue stocks and stock certificates, bonds, notes, and other evidences of indebtedness, payable at periods of more than twelve (12) months.

Kaupulehu Makai Venture intends to transfer the Facilities to KWC in exchange for additional partnership interests in KWC, pursuant to the terms of each Agreement. The transfer of Facilities pursuant to the terms of each Agreement will not involve the issuance of stocks, stock certificates, bonds, notes, or other evidences of indebtedness, payable at periods of more than twelve (12) months after the date thereof; and is not a means of raising funds for the purposes specified in HRS § 269-17. See In re Hawaiian Elec. Co., Inc., Docket No. 05-0084, Decision and Order No. 21821, filed on May 13, 2005, at 12.

---

<sup>34</sup>Consumer Advocate's Statement of Position, Section III, Recommendations, at 17. See also id., Section II(B)(4), at 16.

Accordingly, the commission finds that HRS § 269-17 is inapplicable to the proposed transfer of the Facilities, and the commission's approval pursuant to HRS § 269-17 is not necessary.

B.

HRS § 269-19.5

In general, HRS § 269-19.5 requires a public utility to timely file certain affiliated interest contracts or agreements with the commission, provided that transactions between affiliated Hawaii-based public utilities are exempt from the provisions of HRS § 269-19.5.<sup>35</sup>

HRS § 269-19.5, subsections (c) and (d), state in pertinent part:

(c) . . . provided that all contracts or agreements effective at the time of a general rate proceeding which were discoverable and subject to review by the commission, shall be valid and not subject to subsequent regulatory review and action by the commission; provided further, however, that notwithstanding any other provision to the contrary, there shall be no transfer of real property, or interest in real property between a public utility and an affiliate, without prior approval of the commission, after hearing, wherein the public utility must show that the transfer is in the best interest of the public utility and all of its customers.

No affirmative action is required by the commission in regards to the filing of the contract or agreement; provided however, that if the commission, in its discretion, determines that

---

<sup>35</sup>HRS § 269-19.5, subsection (c), specifies the types of contracts or agreements with affiliated interests a public utility must file with the commission, while subsection (g), specifies a \$300,000 calendar year minimum for HRS § 269-19.5 to apply. KWC previously filed each Agreement with the commission as non-docketed materials, consistent with HRS § 269-19.5.

the terms and conditions of the contract or agreement to be unreasonable or otherwise contrary to the public interest, the commission shall notify the public utility of its determination, whereupon the public utility shall have the option to alter, revise, amend, or terminate the contract or agreement, or assume the risk that future payments for performance of the contract or agreement will be deemed unreasonable and excluded by the commission for ratemaking purposes.

(d) In any proceeding, whether upon the commission's own motion or upon application or complaint, involving the rates or practices of any public utility, the commission may exclude from the accounts of the public utility any payment or compensation to an affiliated interest for any services rendered or property or service furnished, as above described, under existing contracts or agreements with the affiliated interest unless the public utility shall establish by clear and convincing evidence the reasonableness of the payment or compensation.

HRS § 269-19.5(c) and (d) (emphasis added).

The purpose of HRS § 269-19.5 is to:

. . . encourage companies providing essential utility and regulated transport service to Hawaii consumers to obtain their services, supplies, and equipment by relying, to the extent practicable, on competitive procurement practices; provided that when companies obtain their services, supplies, and equipment from affiliated interests, the contracts and agreements between the regulated entity and its affiliates must be shown by clear and convincing evidence to be in furtherance of the interests of the public.

HRS § 269-19.5(b).

KWC is a Hawaii limited partnership, while Kaupulehu Makai Venture, its affiliated interest, is a California general partnership. The proposed transfer of the Facilities includes the transfer of permanent improvements to the land, and thus, involves the transfer of interests in real property between

KWC and its non-Hawaii affiliate, Kaupulehu Makai Venture.<sup>36</sup> Thus, HRS § 269-19.5(c) applies, and the commission's approval following a hearing is required. KWC must show that the proposed transfer of Facilities is in the best interests of all its customers and itself. HRS § 269-19(c).

KWC "waives its right to a hearing on the proposed transfers so long as the transfers are approved by the [c]ommission on the terms proposed by KWC."<sup>37</sup>

KWC asserts that consistent with HRS § 269-19.5(c), the transfer of the Facilities to KWC is in the best interests of its customers and itself:

. . . The transfer of these assets to KWC will be in the best interests of KWC and its customers because (1) the assets are required by KWC in order to provide its water service to its customers, (2) [Kaupulehu Makai Venture] will have divested itself of any direct ownership interests in the assets, leaving KWC in complete control of the assets and insulating the assets from claims that might be made by creditors of [Kaupulehu Makai Venture], (3) following the transfer, the expenses related to these assets to be recovered from KWC's customers will not be significantly different than the expenses that would be included if the assets remained with [Kaupulehu Makai Venture], and (4) the conversion of the value of the assets into equity in KWC will increase its net assets without incurring third party debt if borrowings were required to acquire the assets from [Kaupulehu Makai Venture].

KWC's Statement of Position, at 4; and KWC's Supplemental Written Testimony, at 1 - 2.

---

<sup>36</sup>See KWC's response to PUC-IR-301; and KWC's Statement of Position, at 4.

<sup>37</sup>See KWC's response to PUC-IR-301.

1.

Wells 3 and 4

The maximum volume of potable water KWC is capable of delivering to end users after accounting for reverse osmosis treatment and water line losses is approximately 1,561,140 gpd:

|                     | <u>Capacity</u><br>(in gpd) |
|---------------------|-----------------------------|
| Well 1              | 526,400                     |
| Well 2              | 526,400                     |
| Well 3              | 540,000                     |
| Well 4              | <u>720,000</u>              |
|                     | 2,312,800                   |
| 25% Loss, Treatment | <u>(578,200)</u>            |
|                     | 1,734,600                   |
| 10% Loss Factor     | <u>(173,460)</u>            |
| Net Volume          | 1,561,140                   |

The present average daily water consumption by KWC's consumers is 940,000 gpd. For the test year, KWC estimates 1,033,224 gpd in water sales, with the average daily consumption expected to increase to approximately 1,210,000 gpd by June 30, 2006, the end of the test year. Based on KWC's projected water consumption data, the production capacity from all four (4) wells is needed to meet the anticipated increase in demand for potable water.

The commission finds that the proposed transfer of Wells 3 and 4 is consistent with the best interests of KWC and its customers.

2.

#### Water Treatment Plant

The Water Treatment Plant utilizes reverse osmosis units to remove silicates that naturally occur in the service area's ground water. The reverse osmosis treatment process produces approximately 344,000 gpd of non-potable reject water that is used in the irrigation of landscaping and golf courses within KWC's service area. As part of its rate case, KWC seeks the commission's approval to establish a non-potable reject water rate of \$0.75 per TG.

The commission finds that the proposed transfer of the Water Treatment Plant is consistent with the best interests of KWC and its customers.

3.

#### 413' Reservoir

KWC presently owns three (3) reservoirs with a storage capacity of 1,020,000 gallons. The 413' Reservoir has a storage capacity of 500,000 gallons. Based on the commission's understanding, the storage of water occurs after the water is drawn and undergoes reverse osmosis treatment.<sup>38</sup>

KWC's estimated average daily consumption is 1,033,224 gpd in water sales for the test year. KWC's reservoir storage volume must be equal to the maximum daily water consumption for a twenty-four (24) hour period with no source input to the

---

<sup>38</sup>KWC explains that the water drawn from all four (4) deep water wells flows through the Water Treatment Plant. See KWC's response to CA-IR-24(k). See also KWC's response to CA-IR-28(c).

reservoir, in compliance with Section 111.07(1) of the State of Hawaii, Water System Standards (2002).

Thus, for purposes of storage capacity, the assumed maximum daily consumption is approximately 1,549,837 gpd. The transfer of the 413' Reservoir will increase KWC's storage capacity by 500,000 gallons, to approximately 1,520,000 gallons.

The commission finds that the proposed transfer of the 413' Reservoir is consistent with the best interests of KWC and its customers.

#### 4.

##### Commission's Approval

The commission approves the proposed transfer of the Facilities from Kaupulehu Makai Venture to KWC.

#### V.

##### Orders

##### THE COMMISSION ORDERS:

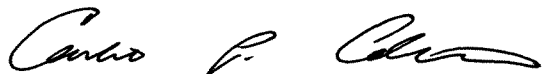
1. The transfer of the Facilities from Kaupulehu Makai Venture to KWC is approved, pursuant to HRS § 269-19.5.

2. HRS § 269-17 is inapplicable to the transfer of the Facilities from Kaupulehu Makai Venture to KWC under the facts and circumstances of this case, as represented by KWC.

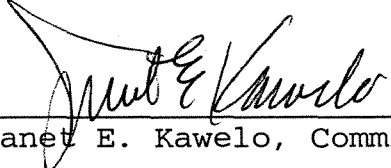


DONE at Honolulu, Hawaii DEC - 9 2005.


PUBLIC UTILITIES COMMISSION  
OF THE STATE OF HAWAII

By   
Carlito P. Caliboso, Chairman

By (EXCUSED)  
Wayne H. Kimura, Commissioner

By   
Janet E. Kawelo, Commissioner

APPROVED AS TO FORM:

  
Michael Azama  
Commission Counsel

05-0124.cs

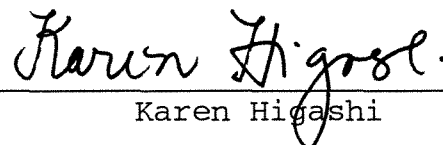
CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the foregoing Decision and Order No. 22178 upon the following parties, by causing a copy hereof to be mailed, postage prepaid, and properly addressed to each such party.

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS  
DIVISION OF CONSUMER ADVOCACY  
P. O. Box 541  
Honolulu, HI 96809

DENISE HILL  
KAUPULEHU WATER COMPANY  
P. O. Box 5560  
Kailua-Kona, HI 96745

ROBERT E. STRAND, ESQ.  
DUANE R. MIYASHIRO, ESQ.  
CARLSMITH BALL LLP  
ASB Tower, Suite 2200  
1001 Bishop Street  
Honolulu, HI 96813

  
\_\_\_\_\_  
Karen Higashi

DATED: DEC - 9 2005